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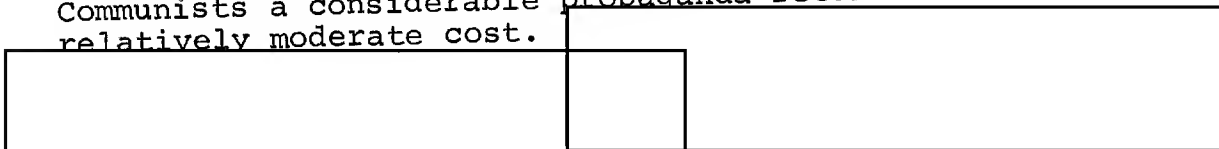
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SOUTH VIETNAM: A growing number of reports suggest that the Communists intend to mount commando-type attacks on selected urban areas during the coming offensive.

Earlier reporting indicated that the fundamental objectives of this offensive will be to damage the pacification program, to inflict defeats on selected South Vietnamese units, and generally to detract from President Nixon's trip to China. The reports suggest the offensive is to involve sizable military campaigns in the highlands and near the DMZ in concert with sapper and guerrilla strikes against selected military targets in the countryside and a few urban areas.

The recent reports, however, indicate that the Communists hope to achieve more of an impact on the urban population by staging a large number of attacks against military compounds near towns and other key targets such as radio stations, utilities, and vital highways and bridges. These operations are to be carried out by newly infiltrated sappers assisted by cadre already in place. According to the latest reports, the enemy is cautioning its forces not to alienate the people by indiscriminate killings and destruction of property.

Among the specific major cities targeted are Saigon, Da Nang, Can Tho, Da Lat, and Qui Nhon. A number of lesser towns, including some district seats, are also listed. It is unlikely that the Communists expect to seize a major city for an extended time. If the enemy can carry off hit-and-run raids, however, such attacks combined with heavier military action in the more remote and less-populated regions of the country, could give the Communists a considerable propaganda return at a relatively moderate cost.



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**USSR-EGYPT:** Yesterday's Soviet-Egyptian communiqué, following President Sadat's three-day visit to Moscow, was little more than a recitation of past Soviet pledges of support. The communiqué also called for "immediate" resumption of the Jarring mission.

The joint statement recorded that the two sides had "again considered measures" aimed at strengthening Egypt's defenses, and had "outlined a number of concrete steps" toward this end. Sadat's public statements before the trip strongly suggested that he would use the occasion to ask the Soviets to supply Cairo with weapons to match Israeli offensive capabilities. He has spoken often of the need to exchange blows with Israel on a "depth for depth" basis. Soviet leaders, however, fear that such weapons would only increase the risk of renewed Arab-Israeli hostilities, which Moscow wants to prevent. The USSR has provided the Egyptians with sophisticated conventional weapons systems without giving Cairo a "retaliatory" capability against Israel.

Earlier Soviet statements in Moscow and at the UN had indicated that the Soviets believe a resumption of UN emissary Jarring's consultations with Arabs and Israelis is the most hopeful approach to a political settlement at this time. Moreover, the Soviets have now countered the US-Israeli agreement for "proximity" talks. Soviet leaders have become increasingly uncomfortable with the US monopoly on efforts to arrange a political settlement, and have stressed that recent US aircraft commitments to Israel have ended Washington's hopes to play an "honest broker" role in the negotiations. In the past few months the Soviets have also resurrected the Soviet peace plan of 1969 to show their Arab clients that Moscow is prepared to become more active in the search for a settlement.

The communiqué may not provide an immediate answer to Sadat's dilemma. The Egyptian president had emphasized that he was going to Moscow to set

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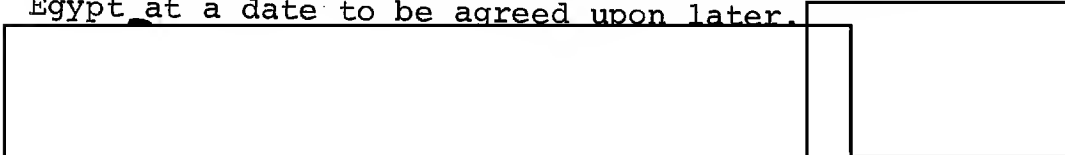
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the "zero hour" for liberating the Sinai. He will return to Cairo without any open expression of Soviet support for a renewal of hostilities, although the language of the communiqué allows Sadat to stress that further military support will be forthcoming.

The joint statement noted that Soviet party chief Brezhnev had accepted an invitation to visit Egypt at a date to be agreed upon later.



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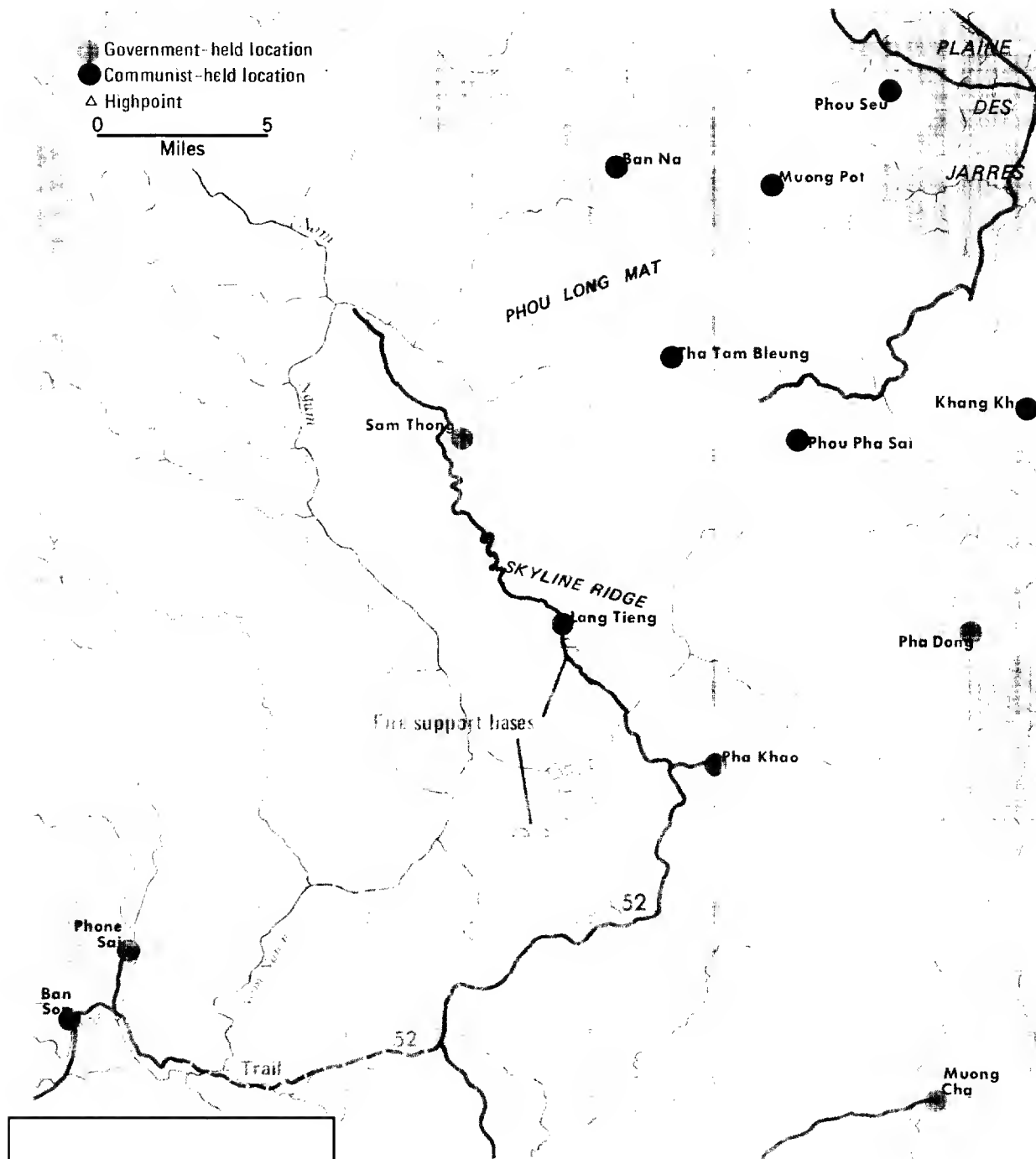
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## LONG TIENG AREA



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**[LAOS:** Lao Communist leader Souphanouvong's latest message to Prime Minister Souvanna makes a bid to resume a dialogue with the government.

The message's reference to earlier Communist demands indicates that there has been no fundamental change in the Communists' negotiating position. It omits, however, any specific call for a US bombing halt in Laos indicating that it was meant to be somewhat more acceptable to Souvanna, who has long insisted that he could not agree to such a halt as a precondition to negotiations.

The message of 27 January reiterates the long-standing Communist formulation that the Lao war must be settled in accordance with the 1962 Geneva Accords and the "realities" of the current situation. The letter states that if Souvanna adopts an "equivalent attitude," the Communists' special envoy would return to Vientiane after a six-month absence to "continue our contacts." Souvanna has indicated that he is drafting a conciliatory response, although once again affirming that he will not knuckle under to Communist demands.

The latest message suggests the Communists may want to probe for some give in Souvanna's position. As in the past, the Communists probably are also interested in projecting a tone of reasonableness at the very time that they are pressing hard militarily.

The government, meanwhile, is continuing to strengthen and redeploy its forces in the Long Tieng area. Four new irregular battalions from Savannakhet are being moved into the Long Tieng area to replace those withdrawn following the recent heavy fighting on Skyline Ridge. The government is continuing to move troops to the Pha Dong area, and by 5 February expects to have some 4,000 men there. The remaining irregular forces--some 8,000 troops--are deployed around the Long Tieng complex from Sam Thong to the new fire support bases in the south.

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COMMUNIST CHINA: The growing strength of the moderate forces in China's unsettled leadership coalition has been affirmed by the reappearance of long-absent politburo member Hsu Shih-yu.

Hsu, a ranking conservative military leader, made his first public appearance in eight months earlier this week at a rally in Kiangsu Province. He was identified as retaining all his previous titles: member of the politburo, commander of the Nanking Military Region, and first secretary of the Kiangsu provincial party committee. Hsu's lengthy disappearance was probably related to the events that precipitated the Lin Piao affair, and his political fate almost certainly has been one of the most controversial personnel issues confronting the regime.

Hsu's reappearance coincides with indications that the political fortunes of other moderate military leaders are on the upswing both at the provincial level and in Peking. Two other conservative military veterans, for example, have been playing a prominent role in Peking since the funeral of former foreign minister Chen I on 10 January. Both these men--Hsu Hsiang-chien and Nieh Jung-chen--were members of the pre - Cultural Revolution politburo who came under heavy radical attack and were subsequently defended by Premier Chou En-lai. Conversely, several civilian radicals on the present politburo have been playing a less active role since the Chen I funeral.

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SOUTH VIETNAM: Economic performance was notably brighter on several fronts in 1971. Although pressures may be more severe this year, Saigon has been showing greater flexibility and resolution in dealing with economic problems.

Real output from agriculture and industry showed a significant increase in 1971. In addition, forestry production, which will be a significant element in export recovery, probably doubled. Although private foreign investment continues to lag, the Japanese showed greater interest in establishing joint industrial ventures in South Vietnam. Additional resources became available to the civilian economy in 1971 in the form of about 20,000 workers released from the US sector, most of whom were absorbed. Localized unemployment exists, however, in the northern provinces.

The rate of inflation was the lowest since 1964, and there was a phenomenal increase in savings in banks and other financial institutions. The interest rate reform of late 1970 resulted in more than a 100-percent increase in time and savings deposits in 1971. Retail prices rose only 14 percent in 1971, compared with increases ranging from 30 to 55 percent during 1965-70. Most of the increase in 1971 occurred during August-December, mainly reflecting some speculative activity prior to the presidential election in October and implementation of major economic reforms, including a devaluation, in mid-November.

At the outset of 1972 it appears that economic problems will mount as a result of increased Communist military activity and the effects of the reduction in the US presence. As the US withdrawal continues, the release of labor from the US sector will become more difficult to absorb. Government expenditures are expected to rise another 25 percent

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while more of the anticipated increase in revenues depends on the very difficult task of increasing domestic tax collections. The Thieu government's much improved performance in economic policy matters in the last 18 months, however, enhances its capacity to cope with these problems.



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EUROPEAN COMMUNITIES: The EC is resuming its efforts to foster monetary cooperation in line with earlier commitments, despite fundamental differences in approach among the member countries.

At a Council meeting earlier this week, EC Commissioner Barre again urged action on monetary questions without which, he stressed, the Community would become "no more than an empty shell." Barre emphasized the need to consider not only the narrowing of margins between Community currencies but also controls on capital inflows and some preliminary formulations of a common reserve management policy--if not yet a pooling of reserves. These issues probably will be brought up at the meeting of the EC central bank governors, scheduled for mid-February, and at the EC Council session of finance ministers which may be held at the end of the month.

The French indicated general approval of Barre's statement. Barre's toning down of earlier suggestions for immediate establishment of a European monetary cooperation fund reflected Paris' objections to supranational institutional arrangements. The Germans, however, maintain their view that monetary cooperation must be paralleled by effective coordination of economic policies. Italy's position represents a middle ground.

While these differences will make progress difficult, the international monetary situation provides a stimulus to common action. Bank of Italy Vice Director General Ossola, for example, holds that EC members' attitudes will be strongly influenced by the behavior of exchange markets during the next few weeks. If the US dollar is trending to the floor in most exchange markets and central banks are purchasing large amounts of dollars, there will be a corresponding heightening of EC interest in taking common monetary measures.

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EGYPT-SUDAN: The purpose of Libyan Premier Qadhafi's surprise visit to Khartoum this week apparently was to ease the strains in Egyptian-Sudanese relations.

25X1 [redacted] the US Mission in Khartoum believes the dispute stems from Numayri's irritation with Sadat's performance during his talks in Moscow last October. According to this account, Numayri, because of the alleged Soviet and local Communist complicity in the effort to depose him last July, took as a personal affront Sadat's call in the Moscow communiqué for closer Arab-Soviet ties. The communiqué also denounced anti-Communist propaganda in the Arab world.

In this frame of mind, Numayri was not receptive to Sadat's insistence that Sudan repair its relations with the Soviet Union and defer the strengthening of ties with the West. Sadat succeeded to the extent that Numayri did not--as had been earlier anticipated--broach the resumption of diplomatic relations with the US during Assistant Secretary Newsom's visit last December. The following week, however, Khartoum re-established ties with West Germany which were severed in 1965. Moreover, Khartoum continues to show a strong interest in expanded economic and cultural relations with the West.

Even if Qadhafi, perhaps with an inducement of financial aid, was able to convince Numayri to make a gesture toward the USSR, the divergence between Egyptian and Sudanese attitudes toward the USSR is likely to remain. Numayri may believe that Sadat no longer supports his retention in power. Moreover, the failure in the past month of Egyptian and Sudanese emissaries to reconcile differences does not augur a rapid normalization of relations.

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DENMARK: Defense reform has been deferred at least until 1973 to permit the nation to focus on the issue of membership in the European Communities.

Parliament began debate of the Social Democratic government's controversial military reform program--one of Prime Minister Krag's five priority programs--on 2 February and then routinely referred it for committee consideration. During the floor debate, the left-wing Socialist People's Party, which provides Krag's minority government its parliamentary majority, spoke against the measure. There were indications, however, that the opposition Radical Liberals might support a modified program. Krag may accept more sweeping modifications in order to achieve a four-party consensus which would include two other opposition "bourgeoisie" parties.

The defense bill probably will not be considered a second time until October--by which time the European Communities issue should be decided.

Krag's reform proposals envisage cutting the standing army from 13,000 to 7,000 men, limiting the navy to small vessels, and stripping the air force of three of its nine tactical units. A reduction in conscription from nine to six months is not part of the reform package but is also under consideration.

NATO is concerned and the Danes have promised to consult the alliance. It is likely that the Danish reform will be scrutinized in the Eurogroup--the UK and all the continental members of NATO except France and Portugal. The US proposal that the Eurogroup undertake such a review has been favorably received initially by a number of Eurogroup members. West German Defense Minister Schmidt, current head of the group, probably will favor placing the item on the group's agenda at a future session.

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VENEZUELA: Minister of Mines Perez has proposed that Venezuela organize a meeting of Latin American oil producing and exporting nations.

Perez believes that Venezuela's experience in dealing with the international oil companies and its familiarity with the market can be useful to other countries in the hemisphere. The Caldera administration is increasingly confident of its ability to dictate terms to the oil companies, having recently asserted a claim to considerable control over these firms through legislation. Regional acknowledgement of Venezuela's lead on petroleum policy could assist Caldera in countering the fear of some domestic critics that he has carried his nationalistic policy too far.

In addition to Venezuela's interest in persuading other countries not to offer the oil companies more favorable conditions than Caracas does, an assertion of leadership on petroleum affairs would be consistent with Caldera's activist foreign policy. Late last year Venezuela organized and hosted a conference of Caribbean foreign ministers to gain support for its own position on the law of the sea issue. Venezuela also has played a vigorous role in the Organization of Petroleum Exporting Countries. The Caldera government probably believes that strong nationalist trends elsewhere in the hemisphere provide a favorable basis for developing a common front by the producing countries in future negotiations with the international companies.

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NICARAGUA: President Somoza has finally agreed to invite OAS representatives to observe Sunday's balloting for the constituent assembly.

Although he had already agreed to the presence of OAS observers for the 1974 general elections, Somoza had resisted opposition pressure for observers during this election. There will be only three to five OAS observers, but Somoza's concession to opposition wishes should have a salutary effect on the electoral climate. His party is the largest in the country and should win easily without fraud or coercion.

An agreement signed by Somoza and opposition leader Aguero early last year guarantees the opposition 40 percent of the constituent assembly seats. The assembly, which will convene in mid-April, will not only revise the constitution but will serve as a legislature during the 30-month interim government. When Somoza's term ends on 1 May, a three-man executive composed of two Liberals from Somoza's party and one member of the opposition Conservative Party, probably Aguero himself, will assume the executive functions.

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WEST GERMANY: Bonn recorded a \$5-billion surplus in its balance of payments for 1971, but losses in the value of reserve assets resulting from the deutschemark revaluation reduced the total to \$3.1 billion. Reflecting the deutschemark's strength during last year's international monetary crisis, large surpluses on short-term and long-term capital account--\$2.9 billion and \$1.7 billion respectively--accounted for most of the over-all payments surplus. The current account, more nearly representative of Germany's competitive position, recorded a surplus of only \$160 million, down sharply from \$770 million in 1970 and \$2 billion in 1969. Rapidly rising foreign worker remittances, estimated at about \$3.6 billion in 1971 (up from \$2.9 billion in 1970), largely offset the trade surplus, which at \$4.9 billion, remained virtually unchanged from 1970.

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LIBYA: Talks between the oil companies and Libya on increased revenues to compensate for dollar devaluation may grow tougher next week when negotiators at the ministerial level take over from technicians. The companies are expected to propose a settlement conforming with the Geneva agreement concluded last month with the Persian Gulf OPEC members. The accord increased Gulf State revenues by about 8.5 percent and contained a provision for renegotiating the price of Persian Gulf oil piped to Mediterranean outlets if a Mediterranean producer achieves a greater increase. Libya, however, has indicated it will seek a larger increase. Libya's usual peremptory tactics may be modified by its sobering experience in attempting to produce and market oil from the British Petroleum operations that were nationalized recently.

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AUSTRALIA: Canberra is making a major effort to stimulate the domestic economy before elections are called later this year. Following moves in December to expand credit, the government has now announced a cut in the interest rate to encourage increased investment spending. Canberra probably will announce additional measures later this month. Rising unemployment and inflation--the major problems facing the economy--and recent cuts in Japanese purchases of Australian raw materials have contributed to the loss of consumer confidence in the economy. The 2.2-percent unemployment rate is small by US standards, but it is a thorny political issue for the government in an election year.

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INTERNATIONAL MONETARY DEVELOPMENTS: The price of gold on the free market fell to \$47 per ounce yesterday afternoon, \$2.25 below the all-time high reached on Wednesday. Moreover, the dollar strengthened vis-a-vis all European currencies. These developments indicate that the markets expect that the United States will soon change the official price of gold to \$38 an ounce now that US and EC negotiators state they have reached agreement on a "balanced package to solve trade problems."

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USSR: The CPSU apparently for the first time is sending a delegation to attend the National Convention of the CPUSA. The relatively high-level delegation, composed of Petr N. Fedoseyev and Nikolay V. Mostovets, will attend the CPUSA's 20th National Convention which opens in Brooklyn on 18 February. Fedoseyev, who has not previously visited the US, is a full member of the Central Committee and Director of its Institute of Marxism-Leninism. He is an important theoretician and has taken relatively conservative positions although he is not regarded as a "hard liner." Mostovets heads the North American Section of the International Department, and as such is responsible for liaison with North American Communist parties.

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